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AUTHOR Meier, Elizabeth L.
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ABSTRACT

Despite many employers' opinions that incentive programs for early retirement are humane and desirable, such programs have several undesirable aspects for the retirees and the U.S. economy. The programs are actually termination programs because they function as a way employers can reduce their work force. (In fact, it was the 1973-75 and 1981-82 economic recessions that stimulated the programs' development, as did industrial structural changes and corporate mergers, deregulation, government agency budget cuts, and growing foreign competition.) Also contributing to the programs' termination-like nature are the facts that early retirees rarely have much choice about whether to retire early and that they often suffer economic losses because of early retirement. The national economy suffers because the programs result in less tax revenue and reduced consumer demand. To help overcome these undesirable aspects of the programs, participants should be entitled to the same access to job placement and other services provided to laid-off employees by employers and the community. Employers should include career planning and job search information in corporate preretirement programs. (The document includes a 40-item reference list.) (CML)

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EARLY RETIREMENT INCENTIVE PROGRAMS: TRENDS AND IMPLICATIONS

by
Elizabeth L. Meier

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The Public Policy Institute was formed in 1985 as part of the Division of Legislation, Research and Public Policy of the American Association of Retired Persons. One of the missions of the Institute is to foster research and analysis on public policy issues of interest to older Americans. This paper represents part of that effort.

The views expressed herein are for informa-
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EXECUTIVE SUMMARY

Early retirement incentive programs are becoming an increasingly common way for employers to deal with the need for work force reductions, particularly in large corporations that already have liberal early retirement provisions in their pension plans. The ages of the employees eligible for these programs dip well below the Social Security early retirement age of 62 - often into the early fifties. Direct costs of these programs are high, particularly when they include an extra "bridge" payment which is made until attainment of the age of eligibility for Social Security, but the costs are expected to be offset by future reduced payrolls. There are other indirect costs caused by the loss of experienced employees which may be incurred in the aftermath of the programs.

Despite the "sweeteners" which are part of early retirement incentive programs, participants often have economic losses not only in foregone wages but in a decrease in the retirement benefit which would have been available at the normal retirement age. While some early retirees obtain other employment or become entrepreneurs, others are not able to find suitable jobs. Early labor force withdrawal for these retirees results in loss of tax revenues and other losses to the economy in the form of reduced consumer demand.

Retirement offers must be voluntarily accepted by eligible older workers as involuntary retirement is prohibited by the Age Discrimination in Employment Act. Nevertheless, the fact that the programs have age and service eligibility requirements - e.g., age 50 with ten years of service - puts pressure on the employees with the requisite amount of age and service. In addition, the environments in which the offers are made are often fraught with uncertainty regarding the future and the time periods for acceptance are short. Under these circumstances, some older workers may feel that they have no choice but to retire despite preferences to continue working.

Recent amendments to the Age Discrimination in Employment Act made mandatory retirement at any age illegal for most private and public sector employees effective January 1, 1987. This and other legislation enables persons to remain in the labor force beyond age 65 as a matter of national policy. At the same time, many private employers, as well as some public employers, are using incentives to encourage workers in their fifties to retire. Under these economic conditions, abolishing mandatory retirement will have diminished impact.

The incentive programs are in reality termination programs rather than early retirement programs which are opted for because of the usual reasons such as ill health or the desire for more leisure. Participants in incentive programs should, then, have the same access to job placement and other services provided by the employer or the community as laid-off displaced workers. Career planning and job search information would be a desirable addition to corporate preretirement programs.

Further study of the impact of early retirement incentives on the income and employment of middle-aged and older workers, as well as the costs of the programs, is needed. More research is required to determine if these programs are generally as humane and desirable as many employers judge them to be, and to examine the alternatives. This study indicates that there are undesirable aspects for older workers, businesses, and the economy.

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I. INTRODUCTION

Increasingly older employees choose early retirement before the normal retirement age stipulated in private pension plans and public employee pension systems. Plan provisions which provide for less than full actuarial reductions to the pension benefit facilitate early retirements, and early retirement incentives accelerate the early retirement choice by older workers. Employers use these incentives - referred to as window benefits - to encourage retirements during a limited period of time or "window" period. The employer's objective is to cut the work force, and the incentives may be part of a more comprehensive employee termination program which includes layoffs and buy-outs by private employers and reductions-in-force in the public sector.

Window benefits provide short-term "sweeteners" to the plan's usual early retirement benefits. The pension plan's eligibility requirements are liberalized by reducing age requirements and/or years of service. Early retirement benefits are also increased through the crediting of additional years of service or by adding a fixed cash amount to the monthly benefit. The latter may be discontinued after the retiree reaches the age of eligibility for Social Security benefits. Some incentive programs offer additional lump-sum cash payments only, which are usually based on years of service.

The incentive programs are a relatively recent development. The 1973-75 and 1981-82 recessions stimulated their use as did industry structural changes such as the massive dismantling and restructuring of the American Telephone and Telegraph Company, and a proliferating number of corporate mergers. Deregulation and growing foreign competition have also forced many companies to downsize their work forces in order to cut costs and thereby become more competitive. In government agencies, budget cuts or changes in program needs require work force reductions. Under these conditions, window programs are used to speed normal attrition among long-service employees who usually receive comparatively high salaries. The programs can be costly to implement but are considered preferable to layoffs and a way to cut labor costs in the long-run.

This paper will explore the incidence and utilization of early retirement incentive programs and the impact on older workers as well as retirement age policy. It has been prepared for the information of all those concerned with the employment of older persons and particularly for AARP's Worker Equity Department.

II. THE ECONOMY AND COMPANY TERMINATION PROGRAMS

Job security is becoming an outmoded concept in today's corporate America. Basic U.S. industries such as steel and oil are fighting to remain alive in the face of foreign competition, disappearing markets and declining prices. Almost every industry, moreover, is affected by deregulation and the increasingly competitive struggle for market shares. Seeking avenues to profitability, many corporations are involved in friendly mergers. Others are the targets of unfriendly takeovers. In 1984, there were 2,543 corporate mergers and acquisitions. The 100 biggest mergers involved firms employing 4.5 million people, or 4.3 percent of the work force. (1) Merger mania continues unabated across the corporate spectrum involving airlines, broadcasting companies, food chains, chemical companies and conglomerates.

Mergers usually result in duplicative or redundant middle management jobs in corporate headquarters in the support services such as human resources and accounting, and anywhere else that jobs are seen as surplus. It was estimated that 20,000 managers lost their jobs as a result of 1984 corporate mergers. (1) In one big oil merger alone, the acquisition of Gulf by Chevron, a total of 20,000 jobs were eliminated between April 1984 and April 1985. (2)

With or without mergers, corporate "downsizing" is the new panacea for profitability. During 1985 and the first half of 1986, nearly 300 companies slimmed down. Some industries are cutting back for the second or third time. (3) Between 1980 and 1985, employment at the nation's 500 largest companies dropped 2.2 million to 14 million. (4) White collar staffs which have been built up in more profitable times are being slashed. New manufacturing processes are being put into place which require the closing of obsolete facilities and the cutting of blue collar jobs. Corporate reorganizations eliminate top and middle managers alike. Under these conditions, the use of early retirement incentives in voluntary termination programs appears to be increasing.

In a recent Towers, Perrin, Forster & Crosby survey of 100 large employers that had offered incentive programs, the economic motive was paramount. Two-thirds of the respondents said that the main objective was to reduce employment levels and costs and avoid layoffs. Twenty employers specified staff redundancy arising from a merger or acquisition, or a change in business direction. Only four said that opening career paths for younger employees was the primary objective. (5) A Hewitt Associates survey also found that economic motives were paramount in offering window plans, but 20 percent of the companies also cited

"more career opportunities needed for younger employees." (39)

Not every company, however, can afford programs which provide expensive "sweeteners" on top of the early retirement provisions of the company's pension plan.* Companies which are in deep economic trouble must take the more direct route of layoffs and firings. In addition, it is usually the larger companies which utilize early retirement incentives because of their ability to finance such programs as well as their likelihood of having pension plans with liberal early retirement provisions. Chart 1 shows that in a study of 400 companies almost 41 percent of the largest companies with 1,000 and more employees had already implemented such programs compared to 13 percent of those with 100-499 employees, and 4 percent of those with 50-99 employees.

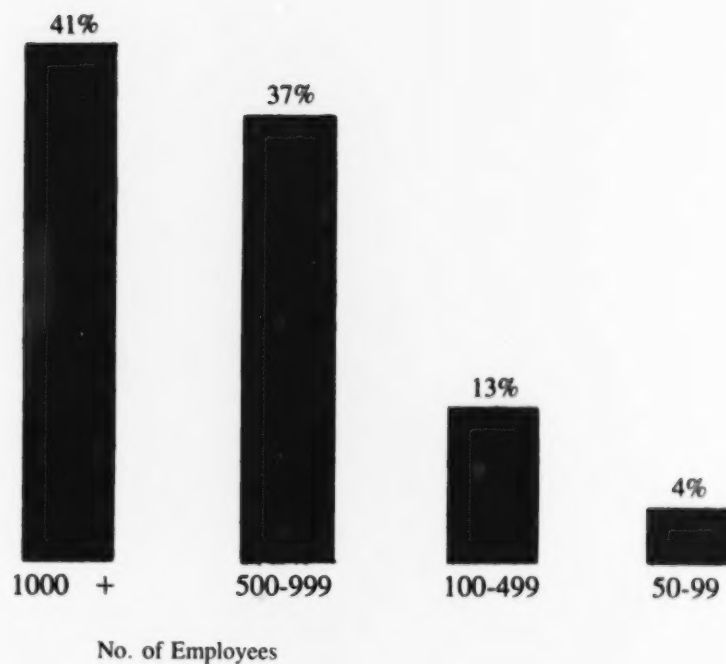
Corporate Programs

The operation, scope and impact of the programs can further be judged by a review of some recent programs in their economic context. The E.I. DuPont deNemours & Co. Inc. offered early retirement programs both as a result of a merger with Conoco Inc. in 1981 and a move into new biomedical products. (6) The acquisition of the oil company was to provide DuPont with a secure source for the oil and gas products needed for its manufacturing plants. (7) It also resulted in an overlap of staff.

Prior to 1985, about 5,000 employees had taken advantage of a voluntary termination program featuring lump-sum payments based on length of service. Early in 1985, DuPont announced an "Early Retirement Opportunity" program whereby as many as five years of credit would be added to an employee's age and service in calculating pensions. All of the employees of domestic operations were eligible with the exception of upper management. It was structured for those workers already eligible for

* The sweeteners to be discussed include pension benefits and lump sum payments only. While many firms also offer continued health benefits, the incidence and type of coverage of health benefits in incentive programs is not included within the scope of this paper.

Chart 1
Percent of Companies That Have Implemented
Early Retirement Incentive Programs
by Size



Source: Yankelovich, Skelly, and White. Unpublished data from a survey of human resources directors conducted for AARP, November 1985.

retirement or for those who would become eligible under the program. The vice president of employee relations said that "other steps," including possible layoffs, would follow if enough employees did not take early retirement. Employees had until April 8 to decide to accept and April 30 to retire. (6) The sweetener offered by the plan made a considerable difference in pension income. An employee age 53 with 22 years of service became eligible for the pension of an employee age 58 with 27 years of service. With an annual salary of \$25,000, the pension would rise to \$675 a month from \$275 a month. (6)

The DuPont plan succeeded in trimming employees beyond expectations. Although between 4,500 and 6,500 workers were expected to retire, more than 11,000 did so. (7) Industry analysts later said that the exodus was an unpleasant surprise to DuPont since it had to hire back several thousand people as consultants for up to a year. (8)

Exxon Corp., the nation's largest oil company, offered an early retirement incentive program to 40,000 of its employees as a result of declining oil prices. Employees had a short window period from April 22 to May 30, 1986, to decide to voluntarily accept the offer. The program was part of a work force reduction and reorganization program which included the establishment of an international organization to manage the company's worldwide interests, consolidating six divisions in the United States and Europe which was announced in March. Almost every U.S. employee, plus overseas employees paid in U.S. dollars, was offered a termination package. Employees 50 and older with more than 15 years of service were offered immediate retirement based on years of service and salary. Three years were added to the years of service and multiplied by 1.6 percent to determine the amount of the retirement benefit. Employees younger than 50 were offered lump sums based on salary and service. (9)

A firm that was conducting two-day retirement counseling seminars for Exxon was asked by employee relations to make it a one-day program and be prepared for groups of about 150 people. Three days after the separation package was offered, the firm conducted its first seminar and in the next two months conducted more than 67 retirement counseling programs.

The company had an employee reduction goal of 15 percent and by program's end achieved a reduction of 15.3 percent, or 6,200 employees. Despite the cuts, layoffs could still be needed because of the uneven nature of the voluntary resignations. Some departments may have lost too many people while others are still overstaffed. A spot-check indicated that those with skills easily transferable to other employers left, including many lawyers and accountants. (9)

DuPont and Exxon are but two of the considerable number of corporate giants that have used early retirement incentive programs to trim the work force. Others have included Union Carbide, Union Pacific, U.S. Steel, Phillips Petroleum, Polaroid, Sears, Nabisco Brands, Kodak, CBS and AT&T. CBS offered an incentive similar to DuPont's, not because of a merger or a takeover, but because the company had lost money fighting off a takeover attempt by Turner Broadcasting. Two Phillips Petroleum programs were also undertaken to help offset the cost of defeating hostile takeover attempts. The first program was offered to employees 58 and over and the second to those between the ages of 55 and 57. A total of 1,930 of the 2,400 Phillips workers age 58 and over accepted the first offer. (10)

Unions are usually receptive to early retirement incentive programs just as they have welcomed and bargained for early retirement pension benefits. Recent collective bargaining agreements have included provisions for incentive programs. For example, in a contract with Caterpillar, the United Auto Workers agreed that the company may opt to reduce the work force by offering a special early retirement supplement of \$300 a month plus the regular early retirement benefit. (11) In another industry, an official of the Bakery, Confectionery and Tobacco Workers Union stated, "Protection for our older members in the form of early retirement incentives ranks high in what we want in agreements with cigarette manufacturers." Agreements reached in 1985 and 1986 contained window benefits. (12) Reflecting a continuing need to downsize after divestiture, AT&T and the International Brotherhood of Electrical Workers included an early retirement 30-day window benefit incentive provision in a new labor contract ratified in July 1986. (13) In August, AT&T offered early retirement to 4,200 service technicians. (14)

Program Costs

Almost all of the programs are undertaken to save money and help the corporations to become more profitable. In the short run, however, incentive programs are expensive. All program costs must be declared as a current expense on the profit and loss statements rather than deferring extra pension costs into the future. This is required by a 1983 standard developed by the Financial Accounting Standards Board (FASB), Financial Accounting Standard No. 74, Accounting for Special Termination Benefits Paid to Employees. The Standard's summary states:

The employer is to recognize special termination benefits as a liability and an expense when the employees accept the offer and the amount can be reasonably estimated. The amount to be recognized includes any lump-sum payments and the present value of any expected future payments. If reliably measurable, certain changes in the estimated costs of other employee benefits are also to be included in measuring the expense. (15)

When the FASB issued an Exposure Draft of the proposed statement on December 28, 1982, the draft prompted a response from one accounting firm that FASB wanted to "shut the open windows" claiming, "The one-shot drain on earnings will deter many employers from even offering window plans. Instead of accounting for management decisions, the new standard would frequently direct them!" (16)

Despite the concern elicited by the exposure draft, employers have not been deterred from implementing window benefits. FAS No. 74 has now been superseded by FAS No. 88 which goes into effect for fiscal years after December 15, 1986. (17) The concept of recognizing current liability when the employee accepts the offer remains. DuPont adopted No. 88 for its 1985 financial statement, and under that Standard the 1985 early retirement window incentive cost \$200 million compared to a previous estimate of \$240 million. (18) Exxon would not put a figure on its program, but its total restructuring cost \$235 million. (9)

The costs of the liberalized pension benefits in the programs vary with the amounts of extra pension credits and the age of the employees accepting early retirement as the present value of the retirement benefit is higher for the younger retirees compared to older employees. Since early retirement incentive programs usually include, and may even be primarily directed to, employees in their fifties, the added cost of these programs compared to normal or actuarially reduced early retirement is considerable. When the monthly pension benefit is

further sweetened by monthly supplements, funding costs are increased. Table 1 illustrates how costs at age 55 compare to costs at older ages. The cost of the same \$1,000 life benefit is \$124,246 at age 55 compared to \$101,494 at age 65 or 22 percent higher. With a \$400 monthly supplement to be paid to age 62, the cost of a life benefit of \$1,000 monthly for an employee retiring at age 55 is \$149,829 or almost 50 percent higher than the cost of the same benefit for an employee retiring at age 65.

TABLE 1

COST TO EMPLOYER OF RETIREE BENEFITS AT DIFFERENT AGES

<u>Age</u>	Retiree Life Benefit Age 62 Supplement		\$1,000 Monthly \$400 Monthly		As % of Age 65 Benefit
	<u>Cost of \$1,000 Life Benefit</u>	<u>As % of Age 65 Benefit</u>	<u>Cost of \$400 Supplement</u>	<u>Total Cost</u>	
55	\$ 124,246	122.4	\$ 25,584	\$149,829	147.6
58	118,010	116.3	16,338	134,348	132.4
60	113,552	111.9	8,850	122,402	120.6
62	108,864	107.3		108,864	107.3
65	101,494	100.0		101,494	100.0

Source: Special Tabulation by William M. Mercer-Meidinger, Inc.
Assumes an Interest Rate of 7.5%

III. PUBLIC EMPLOYEE PROGRAMS

The Federal Government

Normal retirement ages under the Federal Civil Service Retirement System (CSRS) are age 55 with 30 years of service, age 60 with 20 years, and age 62 with 5 years. At these ages an unreduced annuity may be taken at the option of the employee. Statistics compiled by the Office of Personnel Management (OPM) show that the average age of optional retirement under these rules is 61. The CSRS also has special rules (generally for earlier retirement ages) for air traffic controllers, hazardous occupations such as firefighters and law enforcement officers, and for Members of Congress and their staffs. There are no provisions for reduced early retirement annuities except under special circumstances in government agencies such as a reduction-in-force (RIF) or a reorganization. The eligibility requirements for these early retirements are 25 years of service at any age and age 50 with 20 years. There is a two percent a year reduction in the annuity for every year the retiree is under age 55.

Before 1969, early-out authority was not widely used, but was increasingly utilized in the 1970s. The General Accounting Office (GAO) issued a report in 1980 which stated, "At the end of fiscal year 1979, approximately 125,000 or 10.5 percent of all civil service retirees had retired under the early voluntary and involuntary retirement provisions.... About 29,000 of these occurred in 1973 and 1974 when agencywide early retirement authorizations were given to the Department of Defense to ease the post-Vietnam reduction in Federal employment." GAO estimated that the average age of early retirement was 54. (19)

In 1986, as Federal budgetary cuts threatened layoffs, the "Federal Employees' Optional Early Retirement Act of 1986" (S. 2197) was introduced in the Senate. S. 2197 would differ from the existing voluntary and involuntary early retirement authorization authority in that it would extend the authority governmentwide for a limited six month period and would not require imminent RIFs or reorganizations. It would also extend retirement eligibility to two new age and service categories, 15 years of service and age 55, and five years of service and age 57. A prohibition on replacing retirees for five years unless the Office of Personnel Management (OPM) grants an exception was added.

Unlike the private sector early retirement window programs discussed, the proposed legislation did not offer any "sweeteners" such as cash incentives or credits for additional years of service to augment existing voluntary/involuntary

authority. It proposed to simply broaden the age and service eligibility requirements and extend the authority governmentwide for a six month period. No special offer was included for federal employees already eligible to retire, and no employees age 62 and over would be benefited by the legislation.

The Senate Committee on Governmental Affairs held a hearing on the bill on May 15, 1986. Federal union representatives and others who testified before the Committee generally opposed the provisions which provided for the five year hiring freeze and the pension reductions for retiring below age 55. In addition, concern was expressed that a governmentwide program would allow far too many employees to take an early out. As the Director of OPM stated before the Committee:

"... all of us in the Executive Branch are very concerned that a governmentwide early retirement opportunity could lead to excessive losses of our most valuable employees. Under the President's Budget, our civilian workforce would be reduced by about 23,500 in fiscal year 1987--a goal that can be achieved largely or completely by attrition rather than reduction in force--yet the number who might retire in a governmentwide "early out" has been estimated to possibly approach three times that number, and could go much higher. Included in this exodus would be many of our most valuable, and most difficult-to-replace, employees. This would be true even in agencies and programs that are slated to remain fully funded or to grow. This could have a devastating effect on the ability of our managers to manage, and could gravely harm the efficiency and effectiveness of Government, and could even endanger the national defense." (20)

The National Treasury Employees Union pointed out that the penalty for retiring under age 55 "... generally permits employees at the upper end of the grade scale and those who are highly qualified for private sector employment to leave, but precludes early retirement for many low and middle-income employees who cannot afford to retire on a significantly reduced annuity." (21) The union cited an example of an employee age 52, with 27 years of service and an average salary of \$25,000, who would have his annuity cut from \$14,062 at age 65 to \$11,062 at age 52 under the legislation.

In addition to the annuity cut, there would be foregone salary income as is shown by Table 2 which is excerpted from the testimony of the American Postal Workers Union and compares a postal worker who retired at age 50 compared to a worker who retired at age 60. While the amount of the annuity for the

Table 2
PROJECTED RETIREMENT BENEFITS OVER A POSTAL WORKER'S
EXPECTED LIFETIME UNDER THE EARLY OUT OPTION
AND THE CURRENT LAW RETIREMENT OPTION

POSTAL WORKER #3A
AGE AT RETIREMENT: 50 (EARLY OUT)
YEARS OF SERVICE: 20

POSTAL WORKER #3A (NORMAL RETIREMENT)
AGE AT RETIREMENT: 60
YEARS OF SERVICE: 30

HIGH-3 SALARY	BENEFIT IN YEAR OF RETIREMENT		HIGH-3 SALARY	SALARY EARNED FROM AGE 50-60 ^a		BENEFIT IN YEAR OF RETIREMENT	
\$24000.00	1986	\$7830.00	\$34041.00	1986	\$24648.00	1996	\$12339.86
	1987	\$8096.22		1987	\$25313.50	1997	\$12759.42
	1988	\$8436.26		1988	\$26376.66	1998	\$13295.31
	1989	\$8807.46		1989	\$27537.24	1999	\$13880.31
	1990	\$9194.98		1990	\$28748.87	2000	\$14491.04
	1991	\$9590.37		1991	\$29985.08	2001	\$15114.16
	1992	\$10002.76		1992	\$31274.43	2002	\$15764.06
	1993	\$10432.87		1993	\$32619.23	2003	\$16441.92
	1994	\$10881.49		1994	\$34021.86	2004	\$17148.92
	1995	\$11349.39		1995	\$35484.80	2005	\$17886.32
	1996	\$11837.41	TOTAL TEN YEAR SALARY: \$296009.68			2006	\$18655.44
	1997	\$12346.42				2007	\$19457.62
	1998	\$12877.32				2008	\$20294.30
	1999	\$13431.04				2009	\$21166.95
	2000	\$14008.58				2010	\$22077.13
	2001	\$14610.95				2011	\$23026.45
	2002	\$15239.22				2012	\$24016.59
	2003	\$15894.51					
	2004	\$16577.97					
	2005	\$17290.82					
	2006	\$18034.33					
	2007	\$18809.80					
	2008	\$19618.63					
	2009	\$20462.23					
	2010	\$21342.10					
TOTAL BENEFITS OVER LIFETIME:		\$337003.13					\$297815.80
TOTAL BENEFITS AND SALARY AFTER 1986:		\$337003.13					\$593825.48

^aBenefit and salary estimates include COLAs as projected by the Congressional Budget Office, February 1986.
Salary estimates also include adjustments based upon current ACW bargaining agreements.
Source: American Postal Workers, AFL-CIO

person who retired in 1986 would, due to COLAs, be not much less than the similarly situated postal worker when he or she retires at age 60 in 1986, the foregone lost wages which are not replaced by the annuity benefit would be over \$250,000. (22)

Early retirement also is costly for the retirement fund. GAO has estimated that the true actuarial cost of retirement below age 55 is eight percent a year rather than the two percent required by the early out authorization. OPM has contended that it is 6.3 percent. In any case, the cost far exceeds the two percent reduction. Other costs include the loss to the retirement fund of the agency and employee contributions that would otherwise be made. (19)

S. 2197 was revised in July to reduce the five year hiring freeze to three with certain other changes, including a reduction in the window period from six to three months. However, with no major governmental employee layoffs pending, and union and other opposition to the hiring freeze, the bill died in Committee. No further action was taken in the 99th Congress, but similar legislation could be expected next year if layoffs again appear likely, and any imminent RIFs could also trigger existing early out authorization.

State and Local Employee Programs

On the state and local level, early retirement incentive programs have been relatively infrequent. Schools and colleges, police and fire departments, and welfare agencies have far less need than corporate industry to downsize since their services are required despite economic downturns and competition is usually not a factor. Police and fire departments also usually have very early retirement provisions in their pension plans because of hazardous duties.

Nevertheless, demographic trends and budget cuts have stimulated the use of early retirement incentive programs by states and local jurisdictions. New York, Pennsylvania, and Alaska are among the states that have offered incentive programs with liberalized eligibility requirements and/or service credits. Because of declining student enrollments, several Maryland community colleges recently offered incentive bonuses. Officials at the American Association of Community and Junior Colleges said that incentive programs are part of a relatively new trend among community colleges. (23)

IV. AGE DISCRIMINATION ASPECTS

Early retirement incentive programs must be structured to keep away from any suggestion of mandatory or involuntary retirement to avoid suits by eligible older employees. The Age Discrimination in Employment Act (ADEA) as amended in 1986 protects most employees age 40 and over from such actions. Involuntary retirement was specifically addressed in the 1978 ADEA amendments. The involuntary retirement amendment was added as a clause to the ADEA's section 4(f)(2). As the House-Senate Conference Report on the legislation stated, the purpose was to "...make absolutely clear ...that the exception does not authorize an employer to require or permit involuntary retirement of an employee within the protected age group on account of age." (24)

Previous to the amendment, section 4(f)(2) had been the subject of litigation as to whether the law in fact had banned compulsory retirement before age 65, the age cap on protection provided by the statute. As enacted by the Congress in 1967, that section provided that it was not unlawful for an employer:

To observe the terms of a bona fide seniority system or any bona fide employee benefit plan such as retirement, pension, or insurance plan, which is not a subterfuge to evade the purposes of this Act, except that no such employee benefit plan shall excuse the failure to hire an individual. (29 U.S.C. 623(f)(2))

The 1978 Amendment added, "and no such seniority system or employee benefit plan shall require or permit the involuntary retirement of any individual... because of the age of such individual." (24)

Because of the prohibition against involuntary retirement, incentive programs usually include all eligible employees within departments or divisions of a company or in a given geographical location, and emphasize the voluntary nature of participation in the program. But the issue of forced retirement may still arise because of conditions surrounding the offer. As Christopher Mackaronis, the manager of advocacy programs in AARP's Worker Equity Department observes, "The window period may be short and at times rumors tend to fly. Perceived threats of imminent layoffs and talk concerning the 'new' company may lead older employees to believe that they have no choice but to take what's offered and retire." (25)

For some employees there may not, indeed, be a choice. There may not be any job left after the window period is over. As the recent cover story of Business Week stated, "Of course,

if enough volunteers don't step forward, the threat of termination hovers constantly in the air. Combustion Engineering Inc. and Exxon fired hundreds of workers when voluntary programs failed to hit their targets." (3) Should an older worker be fired and feel that the firing was because of age, he or she must file a charge of discrimination under the ADEA and be able to prove that the action was illegal and not based on poor performance. Strict time limitations and procedural requirements must also be met.

Differential Benefits

Another aspect of retirement incentive programs which may give rise to ADEA suits is that of differential benefits. Under section 4(f)(2), employee benefit plans may have differential benefits which either decrease with age or cut off at a certain age if the plan "is not a subterfuge to evade the purposes of this Act." The purpose of this section is to avoid making older workers more expensive to employers (and thus less employable) because of age-related benefit costs. In the Senate debates on the 1978 ADEA amendments, Senator Javits stated, "The purpose of section 4(f)(2) is to take account of the increased cost of providing certain benefits to older workers as compared to younger workers. Welfare benefit levels for older workers may be reduced only to the extent necessary to achieve approximate equivalency in contributions for older and younger workers. Thus a retirement, pension, or insurance plan will be considered in compliance with the statute where the actual amount of payment made, or cost incurred in behalf of an older worker is equal to that made or incurred on behalf of a younger worker even though the older worker may thereby receive a lesser amount of pension or retirement benefits, or insurance coverage." (26)

Welfare benefits are generally benefits such as life and health insurance, but employers have also used the section 4(f)(2) exception in defense of differential exit incentives for younger workers compared to older workers. In one such case, Cipriano v. Board of Education of North Tonawanda, AARP filed an amicus curiae brief in support of the appellants in an appeal. In Cipriano, teachers between the ages of 55 and 60 with 20 or more years of service were offered a lump-sum benefit if they elected to retire during the life of a collective bargaining agreement. The two plaintiffs, age 61, contended that they had been excluded from receiving the benefit solely because of their age. The Association argued "...the undisputed record shows that the retirement incentive was available in the form of a lump-sum cash payment, and that the cost of the benefit bore no relationship to the recipient's age, since recipients between the ages of 55 to 60 would receive the identical \$10,000 amount. Accordingly, the retirement incentive violates the ADEA and is

not the type of plan which Congress intended to protect under section 4(f)(2)." (27)

In addition, AARP argued that the Court had erred in concluding "...that the defendants' retirement incentive 'could not be a subterfuge because it is strictly optional with the employees.'" The "subterfuge" language has consistently been interpreted "...to require an employer to provide equal benefits or incur equal cost for benefits on behalf of all employees, young and old." (27)

In 1986, the Second Circuit Court of Appeals agreed with the applicability of the subterfuge provision. Although the incentive plan appeared to be voluntary, it did not clearly meet the equal benefits or equal cost requirement. The case was sent back to the District Court which was asked to examine why the benefit was eliminated after age 60. This decision does not, however, necessarily mean that the differential benefit issue has been decided as other courts have had conflicting rulings in exit incentive cases. (8)

V. OLDER WORKER IMPACT

The proliferation of early retirement incentive programs adds further impetus to the early retirement trend which became apparent in the 1970s. Although Social Security's age 62 reduced early retirement benefit was authorized for women in 1956 and for men in 1961, it was not until the end of the following decade that there was a sizable drop in labor force participation for the age 60-64 male cohort. In 1970, three-fourths of this age group were in the labor force, but by the end of the decade only 62 percent were employed or looking for work. In the 1980s, decreasing labor force participation by men before age 65 is continuing. This trend for men, as well as the generally counter trend for older women, is shown in Chart 2. The participation increases for the women in their fifties are probably the result of displaced homemakers and other women requiring work income and entering or reentering the work force at midlife. The overall figures mask the labor force behavior of women who have had a long-term commitment to jobs.

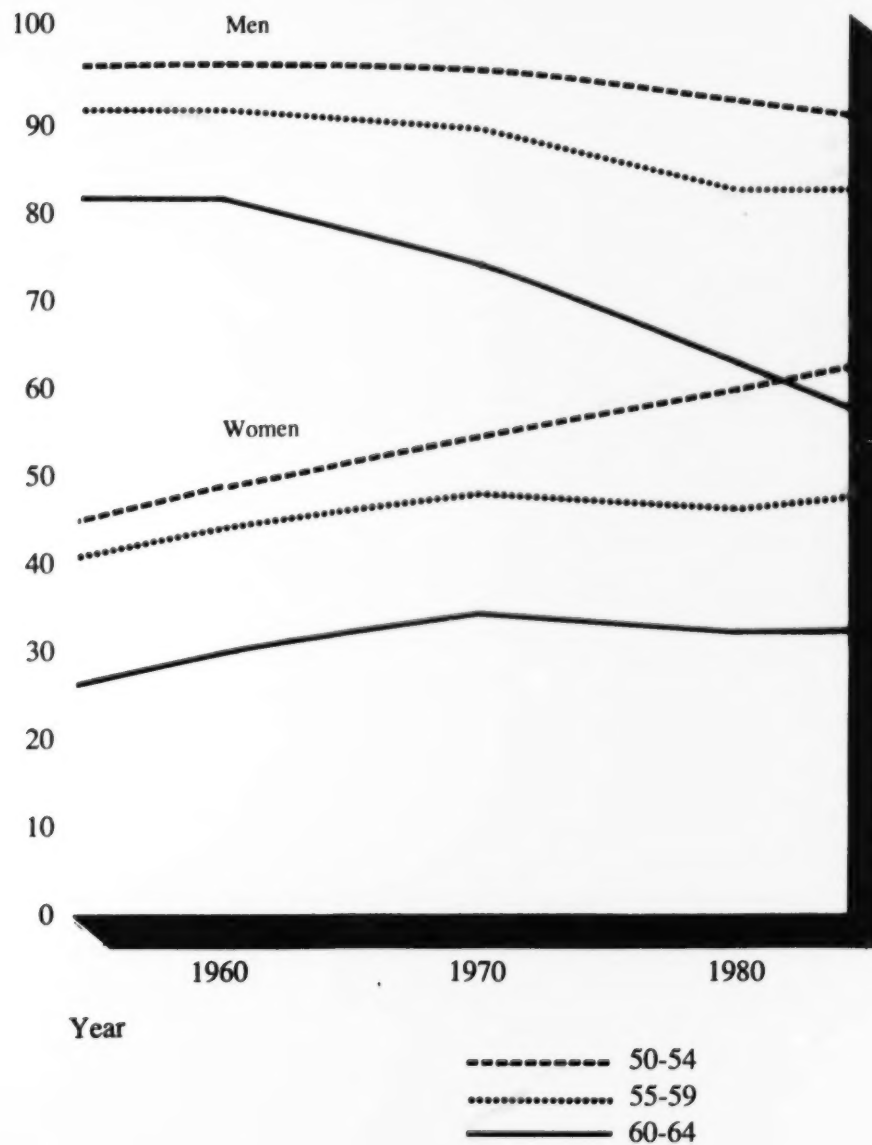
Other studies show that women as well as men retire early. The Social Security Administration conducted a survey of men and women retired worker beneficiaries who received their first benefit in 1980-1981. Sixty-two percent of the women workers compared to almost half of the men workers claimed their benefit at age 62. Seventeen percent of the men and thirty-nine percent of the women had stopped work more than three years before receipt of their first benefit. (29)

Associated with the early retirement trends are increases in private pension receipt at earlier ages due to liberalizations of early retirement plan provisions. Plan participants who began to receive private pension benefits between 1960 and 1969 had a median retirement age of 65, while those who retired in 1977 or 1978 had a median age of 62. (30) The Bankers Trust Company has made a series of studies of plan provisions which show a move beginning in 1965 to liberalize the actuarial reduction of benefits for early retirement. By 1980, most conventional plans did not require a true actuarial reduction at the earliest retirement date. At the same time, among plans using age and service requirements for early retirement, there was a shift towards age 55 from age 60. More recently, the 1980 study showed a new trend; an increasing number of plans are specifying age 50 with a period of service. The minimum service requirement was also reduced from 15 years in 1960 to 10 years. (31)

Targetting Older Workers

Early retirement incentive programs are often described as a

Chart 2
Labor Force Participation Rates
in the Early Retirement Ages
Men and Women, 1960 - 1984



Source: Bureau of Labor Statistics Data. Adapted from General Accounting Office, *Retirement Before Age 65*, Figure 1.1.

"humane" way to avoid layoffs and yet downsize the work force. The Chairman of DuPont, for example, stated "We have been considerate in the way we went about reducing. We tried to preserve the jobs of young people, giving early retirement encouragement to older people Generally, we preserved the employment of young people raising families." (7)

The implicit rationale that older people do not need the jobs to support a family ignores the fact that as early retirement reaches down to those in their fifties the "retirees" may well still have children in school and other family members to support. As people are living longer, older workers may be required to provide some support for an aged parent. The four generations family is on the rise and forty percent of people in their late fifties have a surviving parent. (32) A survey of three firms by the University of Bridgeport's center on aging found that almost a quarter of employees age 40 and over provided some care to elderly relatives and nearly 50 percent were chief providers. (33) In any case, whether or not individual employees have families to support is not relevant to the economic need to cut jobs. The "young family" argument can only be regarded as a rationalization to focus on older employees. A more probable reason for this focus than the lack of families to support is the generally higher salaries received by older employees with long service.

It can be argued that as early retirement incentive programs are voluntary, those who do not wish to retire need not apply. However, the environments in which such offers are made are fraught with tension and uncertainty and the time periods to make a decision are short, often a matter of weeks. Persons in the targetted age groups may feel that they have little choice since they may be laid off later and without the retirement sweetener, particularly when the programs are restricted and not company wide. Surviving in the same job to a later retirement age after the open window is closed may not be easy, especially if the corporate downsizing goals are not met. Nevertheless, there is evidence that a majority of those eligible do not accept a window opportunity. Hewitt Associates found an average acceptance ratio of 36 percent. However, the acceptance ratio in a quarter of the companies was over 75 percent. (39)

Another aspect of the incentive programs and their impact on the older employee population is that the offer may be repeated in the space of a few years. The Hewitt survey covered the period 1981-85 and found that 40 percent of the companies which had offered voluntary separation plans had done so more than once. (39) More recently, one company which is expected to offer another early retirement incentive as part of a restructuring plan has already offered window programs in 1982,

1984 and 1985. (41) Continued emphasis on extra early retirement over the years is bound not only to reduce the number of experienced older personnel but tends to threaten the careers of those who remain since it may be assumed that they will soon have an opportunity for early retirement.

Employment After Early Retirement

Early retirement incentive programs include employees in their fifties or early sixties who generally expect and need to find another job after "retiring." These older workers, particularly white collar employees, stand the best chance of obtaining another job in small and medium-sized firms, since most of the large Fortune five hundred companies are reducing work forces rather than hiring. After decades of experience with one company, however, it is not easy. One placement firm estimated that former corporate managers may have to contact 600 to 900 potential employees before finding a position. (4)

Other retirees try consulting or start their own businesses. Some are successful and some are not. Only a minority of those trying consulting make more than \$10,000 a year. (3) Some of the more successful do business with their former employers or other former corporate contacts. But starting a new business is always risky as the Small Business Administration estimates that only half survive the fifth year. (4) Early retirees who receive lump-sum sweeteners may use the money to capitalize a business but risk losing this financial cushion.

Middle managers employed by 600 corporations were polled on their actions if they were paid off or accepted a package deal to leave voluntarily. Only three percent said that they would start their own business and 88 percent said that they would get another job. A large majority, 78 percent, also said that salaried workers in their fifties or older would have the most trouble adjusting to layoffs or buy-outs compared to those in their thirties or forties. (3)

Older blue-collar workers who are included in early outs or layoffs often have more difficulty than white-collar workers in finding jobs. Members of the United Steelworkers of America have lost 250,000 steel industry jobs since 1980, and a union official estimated that fewer than half of the older workers (over age 40) had found new, full-time jobs. Finding a job with a comparable union wage level is almost impossible. Workers with an average age of 55, who were laid off from the Manville Corporation in 1985-86, found that most of the jobs available, such as fast-food clerks or security guards, paid little more than half their former collectively bargained wages. (35)

Blue-collar workers may also try becoming entrepreneurs rather than accept low-paying jobs. Entrepreneur training programs are springing up in depressed areas in the Midwestern rust belt states, and one such program in Michigan spawned 30 new small businesses. As with white-collar entrepreneurs, blue-collar entrepreneurs may look to their former employers for orders as there is a trend to "outsourcing" or contracting out work to independent contractors to cut costs by the big manufacturers. (35)

Unemployment

Data on duration of unemployment by age invariably show that older workers are unemployed longer than younger workers. Table 3 shows that men ages 55 through 64 had the highest average duration of 26 weeks in 1985. They also had the highest proportion of any age group, 46 percent, unemployed 15 weeks and over.

The General Accounting Office recently studied men and women, age 50 and over, who were receiving employer pensions based on 1984 Census Current Population Survey data. Of those who were in the labor force, male recipients below age 62 had an unemployment rate about twice that of nonrecipients. In the 55 to 61 age range, the unemployment rate was almost 13 percent. GAO concluded that among these younger male pension recipients some who would like to work had difficulty finding new jobs. (36)

GAO also found that the majority of early pension recipients were not in the labor force. Chart 3 compares labor force participation rates for the age 55-61 cohort recipients and nonrecipients who are not as yet eligible for Social Security early retirement benefits. The proportion in the labor force is much less for pension recipients compared to nonrecipients and decreased for both men and women between 1974 and 1984. Just how many of these are discouraged workers who have dropped out of the labor force after fruitlessly looking for employment is unknown.

Retirement Income Impact

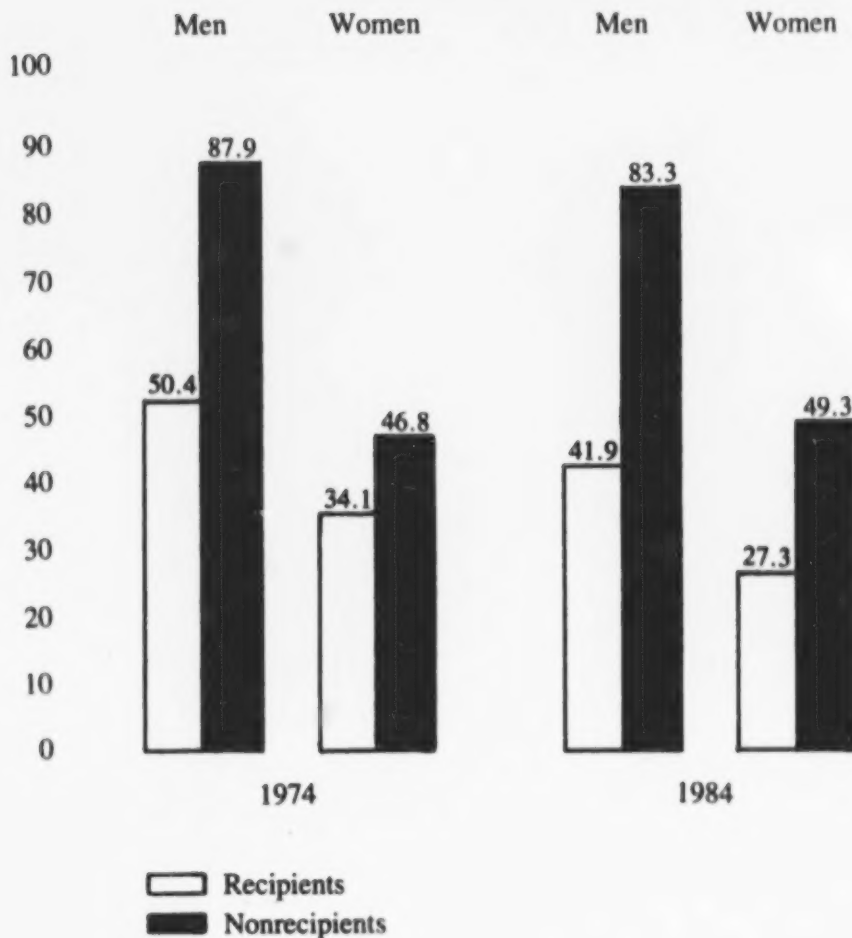
It is unlikely that an older worker who leaves under an early retirement incentive program will become entitled to another pension, particularly from a defined benefit plan. As has been pointed out, the best chance for employment lies in the small business sector of the economy, and small businesses are much less likely than large businesses to offer pension coverage. When they do, it is more likely to be in the form of a profit sharing plan which is, of course, dependent on the profitability of the firm. (37)

TABLE 3
UNEMPLOYED PERSONS, 1985
AVERAGE DURATION IN WEEKS BY AGE AND SEX

<u>Age</u>	<u>Total</u>	<u>Male</u>	<u>Female</u>
Total 16 and Over	15.6	18.0	12.8
16-19	8.0	8.5	7.4
20-24	13.4	15.1	11.2
25-34	16.4	19.1	13.4
35-44	19.1	22.6	15.1
45-54	21.2	24.4	17.0
55-64	22.8	26.0	18.3
65+	19.8	23.3	14.9

Source: U.S. Department of Labor, Bureau of Labor
Statistics. Employment and Earnings.
January, 1986.

Chart 3
Labor Force Participation Rates
for Pension Recipients and Nonrecipients
Men and Women, Ages 55-61, 1974 and 1984



Source: Current Population Survey data from General Accounting Office, *Retirement Before Age 65*, Table 3.2.

For younger employees, the "sweeteners" provided in the early retirement incentive programs help bridge the gap between date of termination and eligibility for reduced Social Security benefits at age 62. They may "age" the person three to five years to bring the person's benefit nearer the benefit expected at the plan's normal retirement age which is frequently age 65, but may be less. Lump-sum payments may also compensate in part for foregone employment income. Yet even the most generous program will usually mean a reduction in pension retirement income compared to the projected benefit at normal retirement age. This is not only because of a reduction in the years of service in the benefit formula but because the final average earnings portion of the formula is likely to be less than if the person had worked additional years and had increased earnings during these years.

The effect of plan termination on the pension benefits of older workers has been studied for AARP by the Policy Center on Aging at Brandeis University, and the findings also apply to older persons who have terminated from a plan, although the effect is mitigated by sweeteners. The study found that in a defined benefit plan which based the benefit on high five-year earnings, the value of the benefit increases 63 percent in the years between age 55 and age 65. This calculation assumes that earnings increase five percent a year. If the age 55 worker would otherwise work until age 65, the combined effect of loss of earnings and years of service on the age 55 worker means that the worker forgoes a 117 percent increase in pension benefits in ten years. (38)

The worker's Social Security benefit may also be reduced if he or she terminates before becoming eligible for a benefit, does not become employed or self-employed, and thus does not have coverage for these years. This is because the benefit is based on covered average earnings, and years without covered earnings generally reduces the average.

Once retired, the terminated workers will probably see the value of their pensions decline as private pensions do not usually provide cost-of-living increases except on an ad hoc basis. The retired workers also will not benefit from any liberalization of the pension plan which occurs between the time of voluntary early retirement and the time that they would normally have retired.

Should the plan be terminated to recover "excess" plan assets or for other reasons, the pension benefit of the retiree could be adversely affected since the possibility of ad hoc benefit increases is then nil. Should the plan be terminated

with insufficient funds, generally because of bankruptcy or other business problems, the benefit payments would be taken over by the Pension Benefit Guaranty Corporation (PBGC) if the plan is insured. While the number of insufficient plan terminations is small, in these plans early retirees could have their benefits reduced since there are limits on the benefits that the PBGC insures. Sweeteners could bring the benefits of early retirees above these limits.

It is apparent that the acceptance of early retirement is not without hazard to participants in the programs. If they expect to obtain other employment, there may be long periods of unemployment because of the difficulty in finding suitable work. If they rely on pension income alone, they may find it inadequate compared to previous expectations of income at normal retirement age.

VI. RETIREMENT AGE POLICY

The Age Discrimination in Employment Act Amendments of 1986, enacted in the closing sessions of the 99th Congress, removed the age 70 cap for all employees 40 and over protected by the law. Mandatory retirement at any age was thus made illegal for most private and public sector employees effective January 1, 1987.* Now most employees age 40 and over are protected against discrimination based on age as a matter of national policy and law.

Apart from the civil rights aspects of the amendments, the driving force behind the legislation was the perceived need to facilitate greater participation in the labor force by older workers. Rising retirement costs and the current and projected aging of the population are factors often cited as reasons for encouraging such participation. These same factors were behind proposals to raise the eligibility ages for receipt of Social Security retirement benefits. The 1983 amendments to the Social Security Act provided that the normal age for receiving retirement benefits will gradually rise from age 65 to 67 after the turn of the century. The early retirement of age 62 is not changed but the reduction for retiring early is increased from the current 20 to 30 percent, thus providing an increased disincentive to retire early.

Another change legislated by the 99th Congress is to require pension plans to accrue benefits for workers age 65 and over. This removed an effective disincentive to work for those covered by pension plans that do not permit continued accruals after age 65.

National policy, then, encourages older persons to remain in the labor force beyond age 65. At the same time, many private employers, as well as some public employers, are using incentives to encourage workers in their fifties to retire. There has been no legislation introduced to stop or discourage this practice. Quite the contrary, legislation was introduced in the 99th Congress to permit a governmentwide early out for federal employees by liberalizing eligibility requirements as has been discussed in Section II of this paper.

*Employees of businesses with less than 20 employees are not covered and certain occupations such as air traffic controllers and airline pilots are exempt. Public safety employees - police and firefighters - as well as tenured college professors, have coverage delayed for seven years.

Short-Run Goals vs. Long-Term Policy

The coexistence of early retirement programs along with a national policy to encourage longer working lives can be explained partly by the fact that early retirement programs are seen as achieving current short-term goals while longer working lives for the work force as a whole is a policy to achieve a future goal. Currently, firms must downsize and cut costs to remain competitive. Governmental agencies want to cut employees because of budget cuts. Early retirement is regarded as less painful than layoffs and therefore popular with employers.

In the short-run, early retirement programs, although costly, are not seen as unduly expensive to the firm when offset by estimated savings in payroll and fringe benefit costs. Pension plans usually have enough funds to support continued reductions in the retirement age without commensurate actuarial reductions.

Inevitably, however, achieving short-term early retirement goals is costly for the economy as a whole and counter to our national retirement policy. While some early retirees will obtain other employment, others will not. The GAO found that 1.3 million pension recipients in the 50-64 age range did not work during 1983 and were retired. If only 25 percent of these retirees went back to work, an additional tax revenue of almost \$1.4 billion would be realized. Further, additional employment would make it less likely that they would later need public welfare expenditures. There would also be secondary effects on the economy through additional consumer demand by individuals remaining in the work force. (36)

The continuing downtrend in private pension retirement ages and reliance on early retirement incentives to cut payrolls act, moreover, as disincentives to both retain and hire older workers in corporate America, and "older" is defined as age 50 and over, not over 65 or 70. In such an environment, removing the mandatory retirement age cap of 70 can hardly be expected to have much impact and the attainment of longer working lives remains, indeed, a futuristic goal.

VII. CONCLUSION

Although early retirement incentive programs are generally seen as a humane way to avoid layoffs, they are, in fact, older worker termination programs. The programs often liberalize age and/or service requirements and make otherwise ineligible persons eligible for retirement during a given window period. This targets a generally younger older worker population in addition to those already eligible under the regular early retirement provisions. It is unlikely that this worker population, as well as those who have not chosen to elect early retirement before, are ready for retirement in terms of complete withdrawal from the labor force. They have not opted for early retirement because of the usual reasons such as ill health or the desire for more leisure.

Involuntary retirement is prohibited under the Age Discrimination in Employment Act, and generally the voluntary nature of the programs is emphasized by employers. The results may or may not meet anticipations. In some instances, the acceptance of the program by too many employees has caused personnel shortages.

Despite the sweeteners contained in the programs, which vary, most participants will have pension benefit loss as well as foregone earnings compared to continued employment until normal retirement age. The further the participant is from that age, the greater the loss. At the same time, the cost to the employer for funding the incentive program is greater for the younger employees compared to their older colleagues.

Some early retirees find other jobs to supplement their retirement income, but the hazards of lengthy unemployment and the inability to find another suitable job are well documented for workers age fifty and over. Those who do find jobs are usually employed by small businesses. Another avenue to employment is entrepreneurship which has a built-in hazard of loss of capital in the event of business failure.

The continued emphasis by corporate America on early retirement well below the Social Security early retirement age of 62 suggests the need for career planning as a part of preretirement planning for corporate employees. Participants in incentive programs should also have the same opportunity to avail themselves of job placement services provided by the employer or the community for laid-off displaced workers.

Further study of the impact of early retirement incentives on middle-aged and older workers is needed. Business restructuring because of competitive pressures, mergers and takeovers is not expected to cease in the foreseeable future and the use of early retirement incentives can be expected to continue. Information on the impact of these programs on the income and employment of eligible workers (both those who participate and those who do not) is fragmentary and more research is needed to determine if these programs are indeed humane and desirable and to examine the alternatives.

Overall, the end result of early retirement incentive programs is shortened work lives for many participants, which is counter to national policy to encourage longer working lives. This is a trend that should not be ignored in assessing retirement age policy.

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